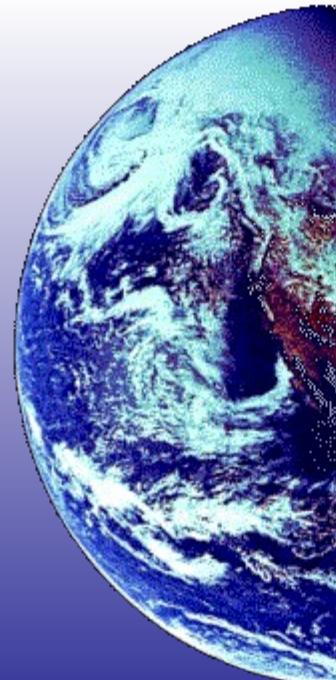




Defense Contract Incentives and the Health of the Defense Industry

**DAEC
October 7, 2003**

Mr. Terry Marlow
Vice President
Government Division

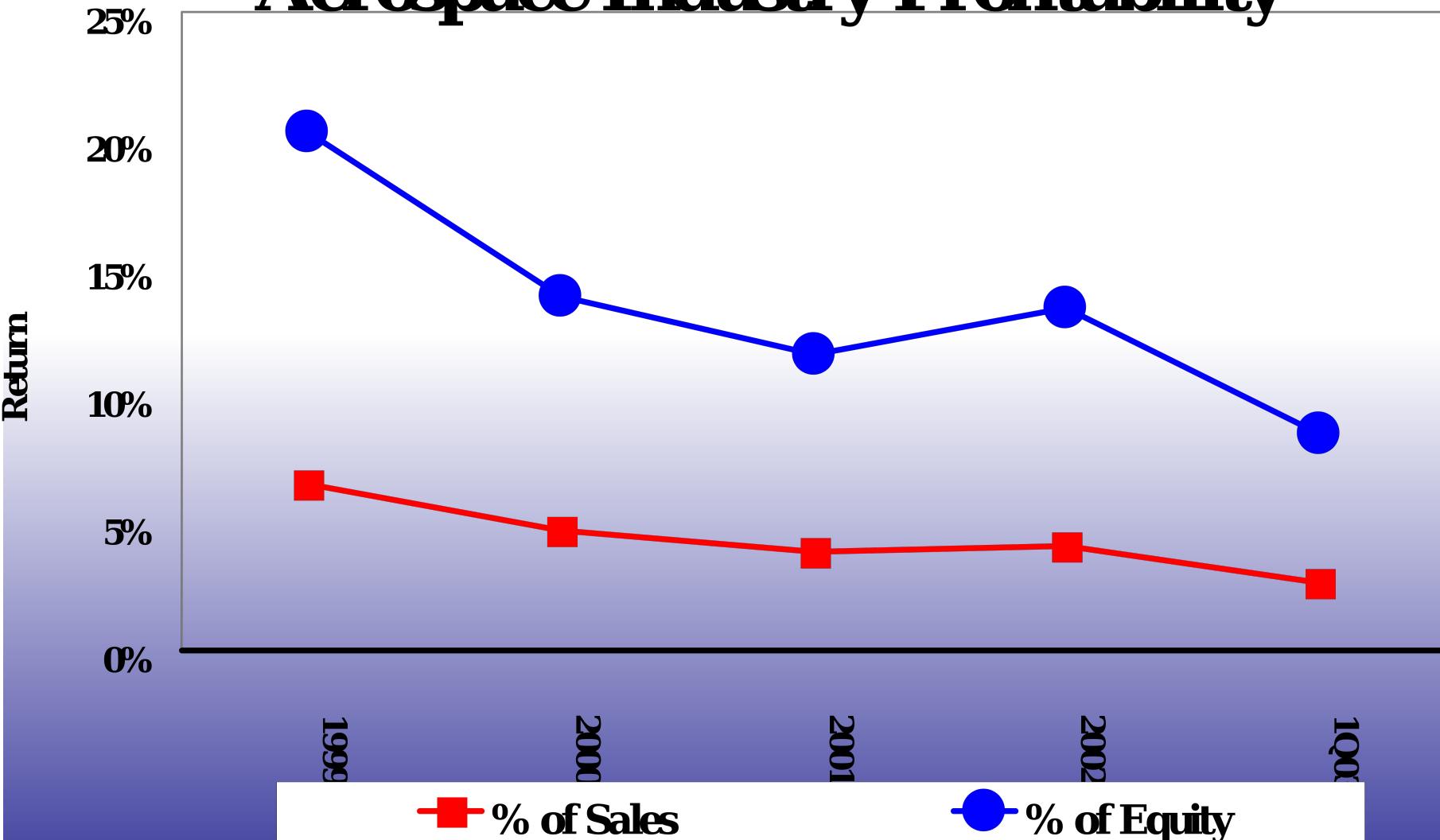




Industry Concern

- Public statements indicate a perception that program cost and schedule growth results primarily from contractors' failure to manage performance
 - Recently issued profit incentive policies may encourage use of high risk contracts too early in program development
 - Some recent award fee provisions may result in zero fees for minimal cost growth on risky development contracts

Aerospace Industry Profitability

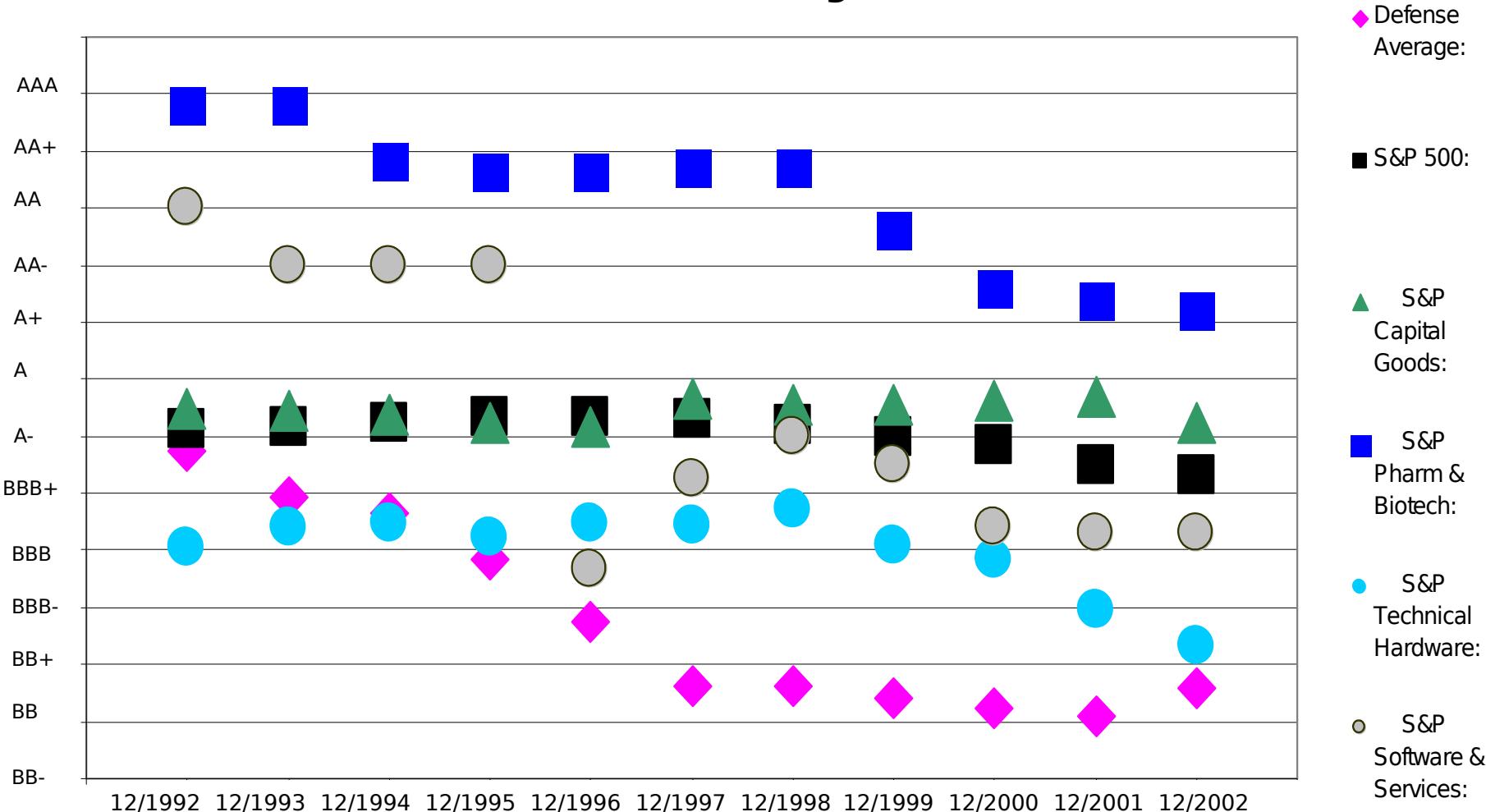




Industry Position

- Industry shares Government's Desire to Minimize Cost and Schedule Growth
 - However, major causes are often beyond contractors' control
 - Requirement changes
 - Unforeseen technical challenges
 - Inadequate budgets
 - Cost estimate optimism in competition

Debt Ratings



Source: Factset, S&P
Compustat, CSIS Analysis



Industry Proposal

- **Government/Industry Collaboration to Achieve Balance in Services' Profit Policies**
- **Aggressive Use of Draft RFPs to Facilitate Discussion of Appropriate Contract Incentives Prior to Implementation in a Competitive Solicitation**
 - Permit changes to draft RFPs to accommodate industry comments
- **We appreciate Navy and Air Force willingness to work with industry to resolve this matter**

